DEPARTMENT OF STATE REVENUE

04-20080074.LOF

Letters of Findings: 08-0074
Use Tax
For the Years 2003, 2004, 2005

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ISSUES

I. Use Tax – Imposition.

Authority: IC § 6-2.5-2-1; IC § 6-2.5-3-1; IC § 6-2.5-3-2; IC § 6-2.5-4-1; IC § 6-8.1-5-1; 45 IAC 2.2-4-1; 45 IAC 2.2-4-2; Sales Tax Information Bulletin 59 (December 2002); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289 (Ind. Tax Ct. 2007).

Taxpayer protests the imposition of use tax on point-of-purchase shelf-edge signs.

II. Tax Administration - Ten Percent Negligence Penalty.

Authority: IC § 6-8.1-10-2.1; 45 IAC 15-11-2.

Taxpayer protests the imposition of the ten percent negligence penalty.

STATEMENT OF FACTS

Taxpayer is a multinational packaged goods manufacturer whose products are sold at retail locations in Indiana. The Indiana Department of Revenue ("Department") conducted a sales and use tax audit of Taxpayer for the years 2003, 2004, and 2005. While no sales tax was assessed against Taxpayer, the Department's audit did assess use tax, penalty, and interest against Taxpayer on several advertising related items. Taxpayer protested several issues including assessment of use tax on certain inserts and invoices with errors. These two issues were resolved in favor of the Taxpayer in consultation with the auditor prior to hearing. A hearing was conducted on the remaining protest issues, and these issues are addressed in this Letter of Findings. Additional facts will be provided as necessary.

I. Use Tax – Imposition.

DISCUSSION

The Department notes that all tax assessments are presumed to be accurate and the taxpayer bears the burden of proving that any assessment is incorrect. IC § 6-8.1-5-1(b), (c); Lafayette Square Amoco, Inc. v. Indiana Dep't of State Revenue, 867 N.E.2d 289, 292 (Ind. Tax Ct. 2007).

Indiana imposes a use tax on the "storage, use, or consumption of tangible personal property in Indiana... regardless of the location of that transaction or of the retail merchant making that transaction." IC § 6-2.5-3-2. The tax is imposed on transactions that occur outside of Indiana that would be taxable if they occurred within Indiana but only if the property is stored, used or consumed in Indiana. IC § 6-2.5-3-1.

IC § 6-2.5-2-1 imposes a sales tax "upon retail transactions made in Indiana" and requires the retail merchant to collect the tax as agent for the State. IC § 6-2.5-2-1. IC § 6-2.5-4-1 defines a retail merchant as one who engages in "selling at retail" and states a person "is engaged in selling at retail when, in the ordinary course of his regularly conducted trade or business, he: (1) acquires tangible personal property for the purpose of resale; and (2) transfers that property to another person for consideration." IC § 6-2.5-4-1(b).

45 IAC 2.2-4-1(a) states, "Where ownership of tangible personal property is transferred for a consideration, it will be considered a transaction of a retail merchant constituting selling at retail unless the seller is not acting as a "retail merchant."

45 IAC 2.2-4-2 states:

> Where, in conjunction with rendering professional services, personal services, or other services, the serviceman also transfers tangible personal property for a consideration, this will constitute a transaction of a retail merchant constituting selling at retail unless:
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> (1) The serviceman is in an occupation which primarily furnishes and sells services, as distinguished from tangible personal property;
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> (2) The tangible personal property purchased is used or consumed as a necessary incident to the service;
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> (3) The price charged for tangible personal property is inconsequential (not to exceed 10 [percent]) compared with the service charge; and
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> (4) The serviceman pays gross retail tax or use tax upon the tangible personal property at the time of acquisition.

The following are the two remaining issues in Taxpayer's protest of the assessment of use tax.

A. Point-of-Purchase Shelf-Edge Signs.

The Department's audit assessed use tax on point-of-purchase promotional signs (POP Signs) on the grounds that Taxpayer was using (leasing) tangible personal property in Indiana, the POP Signs, for which it had not paid sales tax when it transacted for the property. Taxpayer contended that the purchase and distribution of

the POP Signs qualified as a non-taxable promotional service.

Taxpayer contracted with an unrelated entity (CO) to promote some of its products at retail locations, including several retail outlets in Indiana. CO is a developer and marketer of in-store advertising products, programs and services to retailers and consumer goods manufacturers. CO designed, produced, and distributed point-of-purchase promotional signs (POP Signs) for Taxpayer. These are small (generally 4"x 6") promotional signs that are placed in retail outlets on the edge of shelves where Taxpayer's products are located (thus these signs are referred to in the industry as point-of-purchase shelf-edge signs). CO distributes the POP Signs to retailers through its own network of retailers. Promoters, such as CO, compete aggressively to develop their own networks of retailers which then they use to leverage business from packaged goods manufacturers, such as Taxpayer.

Taxpayer pointed to Sales Tax Information Bulletin 59 (December 2002) that discusses the sales and use tax treatment of advertising signs and billboards, and argued that their POP Signs were akin to the billboards in the bulletin examples and therefore their POP Signs transactions should be exempt. The Information Bulletin states:

> The taxability of billboards and advertising signs for sales tax purposes requires a determination of whether the rental of the advertising space is the rental of tangible personal property or the sale of a service. If the rental of the advertising space is the rental of personal property, then the rental is subject to tax. If the transaction of allowing someone to use a billboard or other advertising space is the sale of a service, then the transaction is not subject to tax.
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> The key element in determining whether the transaction is a rental or a service is who controls the property. If the person paying for the use of the advertising space controls the space, the transaction is a rental of the space and is taxable. If the person using the property does not control the property then the transaction is a service.
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> The person paying for the use of the space has control when that person can determine the location of the advertising space or had the right to direct how the advertising space will be used. The person using the space must have exclusive use of the space. Other factors indicating control are whether the customer provides upkeep and maintenance of the space, and whether the customer pays for the posting of the advertising material.
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> EXAMPLES:
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> 1. A person, who owns a portable advertising sign, lets a customer use the sign for one month for five hundred dollars ($500). The customer's employees move the sign to a location determined by the customer and put a message on the sign also determined by the customer. The transaction between the sign owner and the customer is a rental subject to sales tax.
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> 2. A person owns a billboard next to a major highway. The billboard cannot be moved. A customer pays to display an advertisement for thirty days. The customer chooses the advertisement's content but the sign owner employs the people who affix the ad to the billboard. The owners also pays for any upkeep and insurance for the billboard and also owns the property on which the billboard is erected. The transaction is a service because the customer does not control the advertising space.
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> All the materials purchased by a person who provides the service of displaying a customer's advertisements are subject to sales and use tax, including any materials incorporated into the advertising structure itself. All materials purchased to be rented or leased to a customer may be purchased exempt from sales or use tax. (Emphasis added).

Taxpayer's fact pattern does not fall neatly into the fact patterns of the examples provided in Information Bulletin 59 cited above. For one, Taxpayer's facts involve three players: itself, its advertiser (CO), and the retailers that carry its products.

According to Taxpayer and CO (who was also present at the protest hearing) and as documented by the agreement between CO and the retailers in whose stores the POP Signs are placed: the content of the POP Signs is provided to CO by Taxpayer; CO also receives product pricing information from store-specific retailers which it incorporates into the signs; new POP Signs are provided by CO to retailers every two weeks as product promotions change; CO owns the actual shelf-edge components that hold the promotional materials on the retailers' shelves; CO pays the retailers a fee for its use of a retailer's shelf-edge space as well as to have the retailer maintain and replace the signs, and to track sales data before, during, and after the placement and removal of the POP Signs; CO charges Taxpayer a flat fee per POP Sign per store. At the time of the audit, Taxpayer had such displays in 160 stores throughout the state.

These facts diffuse the issue of control that provides the dispositive analysis in the examples presented in the information bulletin. However, for purposes of this Letter of Findings, Taxpayer has provided sufficient evidence, including the contract between CO and the retailers, to show that the control of the tangible personal property used to display its POP Signs is presumptively with CO. CO controls the location of the POP Signs, is responsible for the maintenance of the signs, and owns the display materials. In this instance Taxpayer did not provide a copy of its own contract with CO. Typically this deficiency would have resulted in a denial of Taxpayer's protest for lack of sufficient documentation of its protest. However, the facts as presented tended to support Taxpayer's protest and, therefore, for purposes of this Letter of Findings, this deficiency is outweighed by the other documentation

provided. Taxpayer, however, is on notice that it must provide this crucial document in future audits of its point-of-purchase promotions.

Taxpayer's protest of the assessment of use tax on POP Signs is sustained because Taxpayer is deemed to be purchasing a service and not renting tangible personal property.

B. Advertising Material & Services.

The Department also assessed use tax on Taxpayer's purchase of certain advertising services and materials. Taxpayer states that the Department's audit improperly assessed use tax on the purchase of advertising services.

Taxpayer presented copies of invoices (attached to a letter dated September 17, 2008) that show separate charges under the heading of "Creative Services." Taxpayer is correct, these charges are exempt from use tax, therefore the assessment should be adjusted for invoices with numbers: NE11114, NE10691, NE12764, NE11209, NE11196, NE11192, NE11173, NE11302, NE10691, NE10843, NE12771, NE12797, NE12646, NE11106 (please note that there is a typographical error associated with the last invoice that supplemental review by the auditor acknowledged).

In a follow-up to its original protest, Taxpayer also protested that separate line charges described as "production/traffic/coordination" should also be exempt as separately stated "services." Taxpayer is not correct. IC § 6-2.5-4-1 states in relevant part:

> (e) The gross retail income received from selling at retail is only taxable under this article to the extent that the income represents:
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> (1) the price of the property transferred, without the rendition of any service; and
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> (2) [...] any bona fide charges which are made for preparation, fabrication, alteration, modification, finishing, completion, delivery, or other service performed in respect to the property transferred before its transfer and which are separately stated on the transferor's records.

(Emphasis added).

The charges associated with "production/traffic/coordination" are services performed in respect to the tangible personal property before its transfer. These services are not comparable to the "Creative Services" described above and are not exempt from use tax.

Therefore, Taxpayer's protest under subheading A is sustained. Taxpayer's protest under subheading B is sustained in part and denied in part.

FINDING

Taxpayer's protest of the assessment of use tax on POP Signs is sustained. Taxpayer's protest of the assessment of use tax on charges described on the invoices at issue under the heading "Creative Services" is sustained. Taxpayer's protest of the assessment of use tax on charges described on the invoices as "production/traffic/coordination" is respectfully denied.

II. Tax Administration–Negligence Penalty.

DISCUSSION

The Department issued proposed assessments and the ten percent negligence penalty and interest for the tax years in question. Taxpayer protests the imposition of penalty.

The Department refers to IC § 6-8.1-10-2.1(a), which states in relevant part:

> If a person:
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> . . .
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> (3) incurs, upon examination by the department, a deficiency that is due to negligence;
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> . . .
>
> the person is subject to a penalty.

The Department refers to 45 IAC 15-11-2(b), which states:

> Negligence, on behalf of a taxpayer is defined as the failure to use such reasonable care, caution, or diligence as would be expected of an ordinary reasonable taxpayer. Negligence would result from a taxpayer's carelessness, thoughtlessness, disregard or inattention to duties placed upon the taxpayer by the Indiana Code or department regulations. Ignorance of the listed tax laws, rules and/or regulations is treated as negligence. Further, failure to read and follow instructions provided by the department is treated as negligence. Negligence shall be determined on a case by case basis according to the facts and circumstances of each taxpayer.

45 IAC 15-11-2(c) provides in pertinent part:

> The department shall waive the negligence penalty imposed under IC 6-8.1-10-1 if the taxpayer affirmatively establishes that the failure to file a return, pay the full amount of tax due, timely remit tax held in trust, or pay a deficiency was due to reasonable cause and not due to negligence. In order to establish reasonable cause, the taxpayer must demonstrate that it exercised ordinary business care and prudence in carrying out or failing to carry out a duty giving rise to the penalty imposed under this section.

Taxpayer's Indiana sales were wholesale destination sales made to supermarkets, wholesale grocers, commissaries, and food distributors. A review of Taxpayer's sales tax reporting was found to be in compliance, therefore no sales tax adjustments were made for the audit.

For any remaining issues upon which penalty is assessed, Taxpayer has affirmatively established that its

failure to pay the deficiency was due to reasonable cause and not due to negligence, as required by 45 IAC 15-11-2(c). Any remaining negligence penalty shall be waived.

FINDING

Taxpayer's protest is sustained.

CONCLUSION

Taxpayer's protest of the assessment of use tax on POP Signs is sustained.

Taxpayer's protest of the assessment of use tax on charges described on the invoices at issue under the heading "Creative Services" is sustained.

Taxpayer's protest of the assessment of use tax on charges described on the invoices as "production/traffic/coordination" is respectfully denied.

Taxpayer's protest of the assessment of negligence penalty is sustained.

Posted: 10/28/2009 by Legislative Services Agency
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